June 24, 2014

Fannie Mae Updates Compliance with Laws and Responsible Lending

By Anna DeSimone

June 24, 2014, Fannie Mae published Ann. SEL-2014-07: *Selling Guide* Updates. The *Selling Guide* has been updated to include changes to the following:

- HomePath® Properties
- Incorporate Announcement SEL-2014-05, *Lender Selling Representations and Warranties Framework Updates*
- Federal Home Loan Banks as Grant and Community Seconds® Providers
- 2014 Area Median Incomes
- Miscellaneous *Selling Guide* Update

Two of the updates are described below. Please refer to the 2014-07 Update for additional information.

A3-2-01, Compliance with Laws (06/24/2014)

Introduction

This topic contains information on compliance with laws, including:

- Compliance With Laws
- IRS Reporting Requirements
- Department of Treasury Office of Foreign Assets Control (OFAC) Regulations

Compliance with Laws

The lender (and any subservicer or third-party originator it uses) must be aware of, and in full compliance with, all federal, state, and local laws (e.g., statutes, regulations, ordinances, administrative rules, and orders that have the effect of law, and judicial rulings and opinions) that apply to any of its origination, selling, or servicing practices or other business practices (including the use of technology) that may have a material effect on Fannie Mae. Among other things, this means that the lender must comply with any applicable law that addresses fair housing, fair lending, equal credit opportunity, truth in lending, wrongful discrimination, appraisals, real estate settlement procedures, borrower privacy, data security, escrow account administration, mortgage insurance cancellation, debt collection, credit reporting, electronic signatures or transactions, predatory lending, terrorist activity, ability to repay or the enforcement of any of the terms of the mortgage. Lenders also must ensure that appraisals conducted in connection with single-family mortgage loans delivered to Fannie Mae conform to the *Appraiser Independence Requirements*.

As applicable law can change quickly, and sometimes without widespread notice, the lender must establish appropriate facilities for monitoring applicable legal developments and implementing appropriate measures to stay in compliance with applicable law, and demonstrate satisfactory performance of its legal compliance upon Fannie Mae's request. When a local or state law or regulation represents a potential conflict with Fannie Mae's requirements, the lender must advise its lead Fannie Mae regional office.

A lender may be required to repurchase a mortgage loan that is in breach of the requirements of this topic at any time notwithstanding that the loan is otherwise eligible for relief from enforcement for breaches of certain underwriting and eligibility representations and warranties in accordance with A2-3.2-02, Enforcement Relief for Breaches of Certain Representations and Warranties Related to Underwriting and Eligibility (06/24/2014). Also see A2-2.1-06, Life of Loan Representations and Warranties (06/24/2014), for additional information.

IRS Reporting Requirements

The lender must comply with IRS requirements for:

- Reporting the receipt of $600 or more of interest payments from a borrower,
- Filing statements for recipients of miscellaneous income (IRS form 1099-Misc) to report payments of fees to attorneys for handling liquidation proceedings,
- Filing notices of acquisition or abandonment of secured property (IRS form 1099-A) to report the acquisition of a property by foreclosure or acceptance of a deed-in-lieu or by a borrower's abandonment of a property, and
- Filing notices of cancellation of debt (IRS form 1099-C) to report the cancellation of any part of a borrower's indebtedness.

For specific information about the lender's responsibilities for notifying the IRS about the receipt of interest, payment of fees, acquisition of properties, or cancellation of debt, see the *Servicing Guide*.

Department of Treasury Office of Foreign Assets Control (OFAC) Regulations

Lenders must comply with the Department of Treasury's Office of Foreign Assets Control (OFAC) regulations. All lenders that deliver mortgage loans to and/or service mortgage loans for Fannie Mae must establish and maintain an effective OFAC compliance program. Lenders may not deliver to Fannie Mae any mortgage loan in which the borrower, key principal, or principal is a "specially designated national and blocked person" on the list (SDN List) maintained by OFAC. It is the lender's responsibility to determine and verify that each borrower, key principal and principal is not listed on the most recent OFAC SDN List prior to delivery of the mortgage loan to Fannie Mae.

A3-2-02, Responsible Lending Practices (06/24/2014)

Introduction

This topic contains information on responsible lending practices, including:

- Overview

- Responsible Lending Policies
- Underwriting Standards

Overview

Fannie Mae requires each lender to use prudent, sound, and responsible business practices in its marketing and origination efforts. The lender's operating policies and procedures must provide an effective means of ensuring responsible lending practices, and identifying and avoiding predatory lending practices.

Fannie Mae requires lenders to update their business practices as necessary to ensure continuing responsible lending practices that are in line with current market conditions. Fannie Mae also requires lenders to have policies and procedures, including quality control procedures, to ensure that loans delivered to Fannie Mae comply with these responsible lending requirements. For quality control requirements, see Part D, Ensuring Quality Control (QC).

Responsible Lending Policies

The following summarizes Fannie Mae's policies on responsible lending. As noted below, other sections of the *Selling Guide* provide additional information with respect to Fannie Mae's responsible lending requirements.

Steering

Borrowers should be offered the lowest-cost product with the lowest-risk loan terms for which they qualify. Lenders must not steer borrowers toward a particular loan program to qualify the borrower for a mortgage loan in an effort to misrepresent the borrower's true credit and/or income related qualifications.

Lenders also must ensure that their loan originator compensation practices comply with the loan originator compensation provisions of the Truth in Lending Act and Regulation Z, and that loan originators comply with these requirements when presenting loan options to consumers.

HOEPA Loans

A mortgage loan that is subject to the Home Ownership and Equity Protection Act of 1994 as described in Section 32 of Regulation Z (HOEPA) is not eligible for delivery to Fannie Mae. A mortgage loan that is part of a larger transaction that is structured in a manner intended to circumvent the requirements of HOEPA and Section 32 of Regulation Z is also ineligible for delivery to Fannie Mae.

Single Premium Credit Insurance

Lenders may not require the borrower to purchase, and no proceeds of the mortgage loan may be used to purchase, single premium credit insurance (e.g., life, disability, accident, unemployment, or health insurance) or a single fee debt cancellation agreement. See also B7-3-05, Additional Insurance Coverage (04/01/2009).

Prepayment Penalties
Mortgage loans subject to prepayment penalties are ineligible for sale to Fannie Mae.

Arbitration
A mortgage loan that was originated on or after October 31, 2004, and is subject to mandatory arbitration is not eligible for delivery to Fannie Mae. See also B8-3-02, Special Note Provisions and Language Requirements (08/20/2013).

State Higher-Priced Loans
Certain state-defined higher-priced loans are ineligible for sale to Fannie Mae, regardless of whether the lender is subject to such state requirements as a matter of law. Any state higher-priced loan described in B2-1.4-02, Mortgage Loan Eligibility (04/15/2014), is ineligible for sale to Fannie Mae.

Interagency Guidance on Nontraditional Mortgage Product Risks
A mortgage loan that has a residential loan application date on or after September 13, 2007, and that is a "nontraditional mortgage loan" within the meaning of the Interagency Guidance on Nontraditional Mortgage Product Risks, 71 Fed. Reg. 58609 (Oct. 4, 2006), must comply in all material respects with such guidance, regardless of whether the lender is subject to the guidance as a matter of law.

Statement on Subprime Mortgage Lending (Subprime Statement)
An adjustable-rate mortgage (ARM) loan that has a residential loan application date on or after September 13, 2007, must comply in all material respects with the Statement on Subprime Mortgage Lending, 72 Fed. Reg. 37569 (July 10, 2007), regardless of whether the lender is subject to such statement as a matter of law.

A lender may be required to repurchase a mortgage loan that is in breach of the requirements of this topic at any time notwithstanding that the loan is otherwise eligible for relief from enforcement for breaches of certain underwriting and eligibility representations and warranties in accordance with A2-3.2-02, Enforcement Relief for Breaches of Certain Representations and Warranties Related to Underwriting and Eligibility (06/24/2014). Also see A2-2.1-06, Life of Loan Representations and Warranties (06/24/2014), for additional information.

Underwriting Standards

In addition to complying with applicable legal obligations regarding a borrower's ability to repay, every mortgage loan delivered to Fannie Mae must be underwritten in order to establish that the borrower has the willingness and capacity to repay the debt. Lenders delivering mortgage loans to Fannie Mae should ensure that mortgage loan underwriting standards recognize a variety of factors when evaluating a borrower's capacity to repay a loan. All mortgage loans delivered to Fannie Mae must adhere to the following requirements:

- An analysis of a borrower's repayment capacity must include an evaluation of the borrower's capacity to repay the debt by its final maturity, assuming a fully amortizing repayment schedule based on the term of the mortgage loan.

- The assessment of a borrower's repayment capacity is particularly important if a loan has risk-layering. When risk-layering is involved, the lender must demonstrate the existence of effective mitigating factors that support the lender's underwriting decision and borrower's repayment capacity, and the lender must have clear policies governing the use of risk-layering features. Lenders must not rely solely on one factor to compensate for the risk, but instead must consider a combination of mitigating factors, such as the borrower's credit history, the loan-to-value ratio, the borrower's debt-to-income (DTI) ratio, the borrower's level of reserves and, as applicable, the borrower's prior mortgage payment history.
- Generally, lenders must verify and document the borrower's income (both source and amount), assets, and liabilities used in the underwriting decision for all mortgage loans.
- DTI is a typical method of assessing a borrower's repayment capacity. A lender's analysis of a borrower's DTI must include the total monthly housing-related payments, calculated to include not only principal and interest, but also taxes and insurance, any other property-related assessments (such as HOA dues or co-op fees), in addition to other long-term and significant short-term monthly debts.
- The final mortgage loan application signed by the borrower at closing must include all income and debts of the borrower that were verified, disclosed, or identified during the mortgage process and considered by the lender in the qualification for the mortgage loan subject to the requirements of B3-6-01, General Information on Liabilities (09/20/2010), and B3-6-02, Debt-to-Income Ratios (10/02/2012). Lenders must have adequate internal controls and processes in place to evaluate borrower income and liabilities.

Note: Notwithstanding the foregoing, certain exceptions are made to the above underwriting standards for DU Refi Plus and Refi Plus mortgage loans. See B5-5.2-02, DU Refi Plus and Refi Plus Underwriting Considerations (05/27/2014).

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